THE IMPACT OF CARBON TAX

March 2019

MINERALS COUNCIL
SOUTH AFRICA

A GOOD CAUSE
(THE BATTLE AGAINST CLIMATE CHANGE)

PURSUED THROUGH THE WRONG METHOD
(CARBON TAX)

AT THE WRONG TIME
(A TIME OF ALREADY DEEP FINANCIAL STRESS)

A MARGINAL ENDEAVOUR

Mining in SA is marginal business. A slight increase in input cost results in the closure of some operations.

Unlike other productive sectors, mineral commodity prices are determined by the global market. We cannot transfer increases in costs to the final price of the product.

MINING INFLATION VS SELLING PRICE INFLATION

	Total mining	
Year	Input cost inflation	Selling price inflation
	%	%
2013	10.7	8.9
2014	10.7	(0.8)
2015	6.6	(9.8)
2016	9.0	21.5
2017	6.1	4.4
2018	5.8	1.7
Average	8.2	4.3

Between 2013 and 2018, input costs (measured in rands) have on average increased annually by 8.2% for the overall mining sector, while selling prices have increased by 4.3% over the same period.

AN OVERVIEW OF THE CARBON TAX

The Minerals Council and its members remain committed to sustainable growth of the South African economy and to responsible corporate citizenship.

The previously projected growth rates in the economy have not been realised. South Africa is likely to achieve a reduction in greenhouse gas (GHG) emissions of between 13-14.5% by 2025 & 26-33% by 2035 without a carbon tax. This means that GHG emissions will be below the national benchmark trajectory. This is so particularly in the light of the challenging economic circumstances facing the energy intensive parts of the mining industry due to the downturn in commodity prices.

Supportive of the government's intent to facilitate a transition to a low carbon economy through appropriate policy instruments.

The Minerals Council acknowledges that carbon tax could be one of many policy measures used to promote the behavioural changes necessary to achieve greenhouse gas (GHG) emissions reduction.

However, considering the socio-economic implications of the tax, already falling GHG emissions and also challenges pertaining to the design and the principle set out in the draft Carbon Tax Bill, **the Minerals Council does not support the implementation of the Bill**.

We have rising production costs because our ores must be accessed at greater depths and escalating input costs. Any further increases in costs of doing business through the imposition of carbon tax will further undermine employment levels and decrease employment creation potential.

The socio-economic consequences of implementing the Carbon Tax Bill will be significant, this at a time of already weak economic growth.

The mining industry is already facing immense sustainability challenges.

The additional burden of a carbon tax would threaten the viability of many operations.

Despite the allowances envisaged in phase 1 of the implementation of the Carbon Tax Act the current rate of R120 tons of CO_2 equivalent would be extremely onerous.

Harmony – Doornkop

A HOST OF RISKS AND CHALLENGES – MANY STILL TO BE ADDRESSED

Minerals Council along with BUSA has identified the following concerns and risks with the carbon tax which would hinder its effective implementation.

Lack of policy alignment between the carbon tax and the carbon budget proposed through the draft Climate Change Bill:

There is still no alignment of the carbon tax with the carbon budget system being developed by the Department of Environmental Affairs through the draft Climate Change Bill	The government has assured that the process will be aligned, but to date this has not materialised
Consultation on the post-2022 regime has been promised but still no discussions have begun, which perpetuates a situation of limited business investment This hinders further planing for future tax liabilities.	Concerns pertaining to administration of carbon tax through the Custom and Excise Act: • Non-alignment between the carbon tax period and accounting period of the C&E act

Critical issues essential for the effective implementation of the tax are necessary for providing policy certainty:

GHG reporting system has not been finalised. This is required for verification of GHG emissions. And there is misalignment between the GHG reporting entity and carbon taxpayers	The Renewable Energy Premium has not been published, impacting on the full understanding of costs from a pass through of costs perspective

Significant uncertainty remains for taxpayers in determining their liability, as regulations regarding allowances are still outstanding:

Carbon Offsets Regulations are still under consultation	Two regulations – Performance Benchmarks and Trade Exposure – have not been released for consultation

COMPARATIVE INTERNATIONAL EXPERIENCE

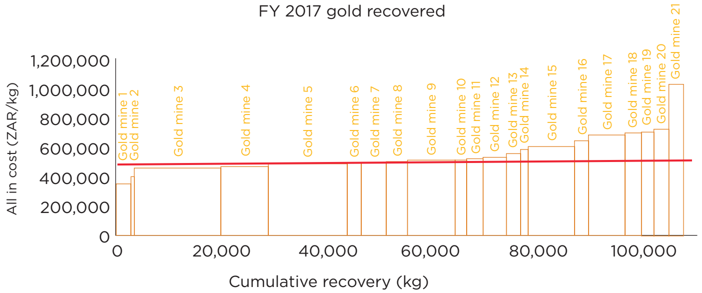
Almost without exception, countries that have implemented carbon pricing systems have done so in a manner that has allowed companies to be exposed to a near-zero cost of carbon during the first phase of implementation. This is done to ensure that companies have time to adjust to the new regulatory environment and can prepare for the cost burden imposed by carbon pricing on their business. The most common tool used in this regard is the free issuance of allowances in emission trading schemes. Taking into account the current state of the mining sector, a 100% relief allowance and a near zero tax rate, should be considered in phase 1.

Glencore – Tweefontein Colliery

VERY TOUGH TIMES FOR GOLD AND PLATINUM MINES

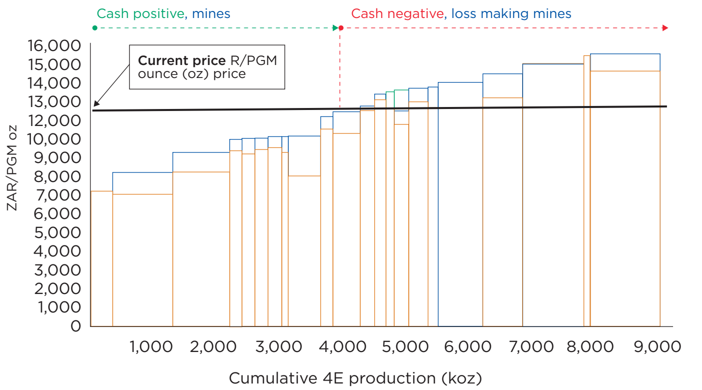
A carbon tax will push some over the edge

Gold industry cost curves (gold price = R529,256/kg)



Source: Minerals Council and Company Annual Financial Statements

Platinum industry cost curves



Source: Minerals Council, Company Annual Financial Statements

These graphs show the status of the gold and platinum group metal (PGM) sectors in 2017. Due to depressed global commodity prices and high input costs, 69% of gold mining operations and 52% of PGM mining operations were producing unsustainably. A change in their fortunes would need either an increase in commodity prices and/or managing input costs downward.

The carbon tax will mean a blanket increase in costs for mining companies. These two sectors employ 287,970 people directly – 62% of the total mining sector. On the sample of companies in the table, the carbon tax will either push the unsustainable operations deeper into the negative or reduce the profitability of those producing sustainably.

IMPACT OF THE CARBON TAX – OUR ECONOMIC MODELLING

10 cents/L CO_2 tax on liquid fuels – mining sector impact

Mining sector direct employment
Total = 462,871 (2017)
10c/L CO_2 tax: 459,168

Indirect employment
Total = 1,305,111 (2017)
10c/L CO_2 tax: 1,294,670

Sector	Total	10c/L CO_2 tax
Primary sector	Total: 17,705	10c/L CO_2 tax: (142)
Secondary sector	Total: 343,926	10c/L CO_2 tax: (2,751)
Tertiary sector	Total: 343,480	10c/L CO_2 tax: (2,751)
Mining	17,505	10c/L CO_2 tax: (142)
Manufacturing	360,954	10c/L CO_2 tax: (2,888)
Wholesale & retail	148,570	10c/L CO_2 tax: (1,189)
Agriculture	0	
Utilities	130,222	10c/L CO_2 tax: (1,042)
Transport & storage	536,977	10c/L CO_2 tax: (4,296)
Construction	6,248	10c/L CO_2 tax: (50)
Finance & insurance	245,413	10c/L CO_2 tax: (1,961)
Community & personal services	12,798	10c/L CO_2 tax: (1,042)

No. of jobs lost as a result of the 10c/L CO_2 tax: 10,441
Less jobs retained because of the diesel fuel refund: 3,605
Net jobs losses: 6,836

- The mining sector has a jobs multiplier of 2.8, one of the highest in the South African economy
- People employed as a result of the mining sector's backward linkages were more than 1.3 million in 2017
- Most indirect jobs were in transport sector (536,977 in 2017)

Impact of the 10 cents per litre CO_2 tax

- Instead of employing 462,871 people in 2017 the sector would have employed 459,168
- Indirect jobs would have been 1,294,670 instead of 1,305,111, a 10,441 decline
- As expected, jobs would have declined by 4,296 in the transport sector
- The gross job losses would have been 10,441 in 2017
- However, net jobs would have been 6,836
- The diesel fuel tax refund offers a major cushion in terms of the number of jobs that could have been lost
- Combustion Emissions Tax through the use of diesel

Kumba Iron Ore – Kolomela Mine

IN CONCLUSION...

While the Minerals Council embraces the notion of long-term carbon pricing and various mechanisms to facilitate transition to a low carbon economy, we are of the view that the carbon tax has the potential to erode profitability through increasing costs and hence result in a shrinking sector.

The result of which would be further job losses, which would further exacerbate South Africa's structurally high unemployment rate.

NOTES

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